

Internal Revenue Service
Appeals Office
8701 S. Gessner
MC 8000 H-AL,
Houston, TX 77074

Number: **201146023**
Release Date: 11/18/2011

Date: August 24, 2011

Department of the Treasury

Person to Contact:

Employee ID Number:
Tel:
Fax:

Refer Reply to:

In Re:

Form Required to be Filed:

Tax Period(s) Ended:

UIL: 501.03-30

Certified Mail

Dear :

This is a final adverse determination as to your exempt status under section 501(c)(3) of the Internal Revenue Code (IRC). It is determined that you do not qualify as exempt from Federal income tax under IRC Section 501(c)(3) effective March 1, 2005.

Our adverse determination was made for the following reasons:

You are not operated exclusively for charitable, educational, or other exempt purposes. You did not engage primarily in activities which accomplish one or more of the exempt purposes specified in section 501(c)(3). More than an insubstantial part of your activities were in furtherance of a non-exempt purpose..

Contributions to your organization are not deductible under Code section 170.

You are required to file Federal income tax returns on the form indicated above. You should file these returns within 30 days from the date of this letter, unless a request for an extension of time is granted. File the returns in accordance with their instructions, and do not send them to this office. Processing of income tax returns and assessment of any taxes due will not be delayed because you have filed a petition for declaratory judgment under Code section 7428.

If you decide to contest this determination under the declaratory judgment provisions of Code section 7428, a petition to the United States Tax Court, the United States Court of Claims, or the district court of the United States for the District of Columbia must be filed within 90 days from the date this determination was mailed to you. Contact the clerk of

the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.


You also have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Taxpayer Advocate Service

Phone:

See the enclosed Notice 1214, Helpful Contacts for Your "Notice of Deficiency" for additional Taxpayer Advocate telephone numbers and addresses.

Sincerely,

A handwritten signature in black ink that reads "Karen A. Skinder". The signature is fluid and cursive, with a long, sweeping underline.

KAREN A. SKINDER
TEAM MANAGER

cc:
Enclosures:

Internal Revenue Service

Department of the Treasury

TE/GE EO Examination
1100 Commerce St. Mail Code 4957:DAL
Dallas, TX 75242-1027

Date:

ORG
ADDRESS

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Certified Mail - Return Receipt Requested

Dear :

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Renee B. Wells
Acting Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG EIN 990		Year/Period Ended 20XX02

LEGEND

ORG - Organization Name XX - Date Address - address City - city
State - state

Issue:

Whether exempt organization qualifies for exemption under Section 501(c)(3) of the Internal Revenue Code.

Facts:

ORG (ORG) was incorporated under the laws of the State of State on March 12, 19XX. In a determination letter dated February 27, 20XX, ORG was determined to be exempt from federal income tax as an organization described in IRC Section 501(c)(3). ORG is located at Address, City, State.

In its Articles of Incorporation, ORG stated its mission was "to improve the lives of individuals and families through better credit counseling, financial management education, including credit restoration and correction procedures.

In its application for exempt status, Internal Revenue Service Form 1023, ORG stated that its activities would consist of providing credit counseling services to low income and indigent individuals and the conducting of community seminars to assist individuals in restoring good credit. According to the Form 1023, volunteer staff would be utilized in these activities.

Activity Description

The CEO of ORG conducts a radio broadcast which invites listeners to call in to ask questions about credit issues.

In addition, a website under the ORG name provides information about the organization, access to archived radio broadcasts, and contact information.

According to the website, ORG provides "credit file restoration, correction with settlement(s), education, and credit file clean-up." To access these services, a fee is required (currently \$ for single persons and \$ for married couples). This fee will generate a "professional credit evaluation." The Executive Director indicated that occasionally these fees are waived in hardship cases at the discretion of the Executive Director (CEO).

After the credit evaluation is prepared, a fee schedule and contract is provided the client which details which credit services such as foreclosures, student loans, and late payments to creditors will be provided.

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A review of the financials provided by the organization as well as the Form 990, *Return of Organization Exempt from Income Tax* for the year under exam, indicated that 100% of the support provided ORG was derived from these fees.

The Credit Counselors are not volunteers but are paid based on a percentage of fees collected from the clients.

A review of the job description for the credit counselors indicates that contrary to a response from the Executive Director as related by the POA in a memo dated October 26, 20XX, education is but a small part of the counselors' responsibilities.

Law:

Section 501(a) of the Internal Revenue Code provides that an organization described in section 501(c)(3) is exempt from income tax. Section 501(c)(3) of the Code exempts from federal income tax corporations organized and operated exclusively for charitable, educational, and other purposes, provided that no part of the net earnings inure to the benefit of any private shareholder or individual. The term charitable includes relief of the poor and distressed. Section 1.501(c)(3)-1(d)(2), Income Tax Regulations.

The term educational includes (a) instruction or training of the individual for the purpose of improving or developing his capabilities and (b) instruction of the public on subjects useful to the individual and beneficial to the community. Treas. Reg. § 1.501(c)(3)-1(d)(3). In other words, the two components of education are public education and individual training.

Section 1.501(c)(3)-1(a)(1) of the regulations provides that, in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. The existence of a substantial nonexempt purpose, regardless of the number or importance of exempt purposes, will cause failure of the operational test. *Better Business Bureau of Washington, D.C. v. U.S.*, 326 U.S. 279 (1945).

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Educational purposes include instruction or training of the individual for the purpose of improving or developing his capabilities and instruction of the public on useful and beneficial subjects. Treas. Reg. § 1.501(c)(3)-1(d)(3). In *Better Business Bureau of Washington D.C., Inc. v. United States*, 326 U.S. 279 (1945), the Supreme Court held that the presence of a single non-exempt purposes, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. The Court found that the trade association had an "underlying commercial motive" that distinguished its educational program from that carried out by a university.

In *American Institute for Economic Research v. United States*, 302 F. 2d 934 (Ct. Cl. 1962), the Court considered the status of an organization that provided analyses of securities and industries and of the economic climate in general. The organization sold subscriptions to various periodicals and services providing advice for purchases of individual securities. Although the court noted that education is a broad concept, and assumed for the sake of argument that the organization had an educational purpose, it held that the organization had a significant non-exempt commercial purpose that was not incidental to the educational purpose and was not entitled to be regarded as exempt.

The Service has issued two rulings holding credit counseling organizations to be tax exempt. Rev. Rul. 65-299, 1965-2 C.B. 165, granted exemption to a 501(c)(4) organization whose purpose was to assist families and individuals with financial problems and to help reduce the incidence of personal bankruptcy. Its primary activity appears to have been meeting with people in financial difficulties to "analyze the specific problems involved and counsel on the payment of their debts." The organization also advised applicants on proration and payment of debts, negotiated with creditors and set up debt repayment plans. It did not restrict its services to the needy. It made no charge for the counseling services, indicating they were separate from the debt repayment arrangements. It made "a nominal charge" for monthly prorating services to cover postage and supplies. For financial support, it relied upon voluntary contributions from local businesses, lending agencies, and labor unions.

Rev. Rul. 69-441, 1969-2 C.B. 115, granted 501(c)(3) status to an organization with two functions: it educated the public on personal money management, using films, speakers, and publications, and provided individual counseling to "low-income individuals and families." As part of its counseling, it established budget plans, i.e., debt management plans, for some of its clients. The debt management services were provided without charge. The organization was supported by contributions primarily from creditors. By virtue of aiding low income people, without charge, as well as providing education to the public, the organization qualified for section 501(c)(3) status.

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In the case of *Consumer Credit Counseling Service of Alabama, Inc. v. U.S.*, 44 A.F.T.R.2d 78-5052 (D.D.C. 1978), the District Court for the District of Columbia held that a credit counseling organization qualified as charitable and educational under section 501(c)(3). It fulfilled charitable purposes by educating the public on subjects useful to the individual and beneficial to the community. Treas. Reg. § 1.501(c)(3)-1(d)(3)(i)(b). For this, it charged no fee. The court found that the counseling programs were also educational and charitable; the debt management and creditor intercession activities were "an integral part" of the agencies' counseling function and thus were charitable and educational. Even if this were not the case, the court viewed the debt management and creditor intercession activities as incidental to the agencies' principal functions, as only approximately 12 percent of the counselors' time was applied to debt management programs and the charge for the service was "nominal." The court also considered the facts that the agency was publicly supported and that it had a board dominated by members of the general public as factors indicating a charitable operation. See also, *Credit Counseling Centers of Oklahoma, Inc. v. United States*, 79-2 U.S.T.C. 9468 (D.D.C. 1979), in which the facts and legal analysis were virtually identical to those in *Consumer Credit Counseling Centers of Alabama, Inc. v. United States*, discussed immediately above.

The organizations included in the above decision waived the monthly fees when the payments would work a financial hardship. The professional counselors employed by the organizations spent about 88 percent of their time in activities such as information dissemination and counseling assistance rather than those connected with the debt management programs. The primary sources of revenue for these organizations were provided by government and private foundation grants, contributions, and assistance from labor agencies and United Way.

Outside the context of credit counseling, individual counseling has, in a number of instances, been held to be a tax-exempt charitable activity. Rev. Rul. 78-99, 1978-1 C.B. 152 (free individual and group counseling of widows); Rev. Rul. 76-205, 1976-1 C.B. 154 (free counseling and English instruction for immigrants); Rev. Rul. 73-569, 1973-2 C.B. 179 (free counseling to pregnant women); Rev. Rul. 70-590, 1970-2 C.B. 116 (clinic to help users of mind-altering drugs); Rev. Rul. 70-640, 1970-2 C.B. 117 (free marriage counseling); Rev. Rul. 68-71, 1968-1 C.B. 249 (career planning education through free vocational counseling and publications sold at a nominal charge). Overwhelmingly, the counseling activities described in these rulings were provided free, and the organizations were supported by contributions from the public.

Government's Position:

The purpose of ORG's activities differ substantially from those of the organizations in

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Rev. Rul. 65-299, Rev. Rul. 69-441, and Consumer Credit Counseling Service of Alabama, Inc. In this case, ORG engages in minimal activities which further an exempt purpose. Furthermore, no public financial support is provided.

Conclusion:

Based upon the information noted above, it is proposed the exempt status of the organization be revoked effective March 1, 20XX. Form 1120, U.S. Corporation Income Tax Return should be obtained for the year ended February 28, 20XX, and for future tax years.